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IN THE

Supreme Court of the United States.

No. . October Term, 1932.

THE TRAINOR COMPANY,
Petitioner,

v.

THE AETNA CASUALTY AND SURETY CO.,
Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT.

To the Honorable, the Chief Justice and the Associate Justices of the Supreme Court of the United States:

Your petitioner, The Trainor Company, respectfully shows to this Court as follows:

ORIGIN AND NATURE OF THE CASE.

This is a petition for a writ of certiorari to the United States Circuit Court of Appeals for the Third Circuit to review its decision affirming the action of the United States District Court for the Eastern District of Pennsylvania in restricting the plaintiff's judgment to nominal damages. The decision of the Circuit Court of Appeals was filed December 21, 1932, and appears at page 63 of the record. It has not yet been officially reported. The opinion of the District Court is found on page 31 of the record, and is officially reported in 49 F. (2d) 769.

This is an action of assumpsit brought by the plaintiff as obligee against the defendant upon a bond guaranteeing the completion of a building operation. Suit was originally brought in the Court of Common Pleas of Philadelphia County and later, by agreement, was supplanted by this suit in the United States District Court for the Eastern District of Pennsylvania. The bond recited that the principal, Copley Homes Inc., was indebted to the plaintiff in the amount of $28,000, being the balance of the purchase price due the plaintiff for fifty-two lots of ground which the plaintiff conveyed to Copley Homes Inc.; and that it desired the plaintiff to accept in payment an equity in a second mortgage secured on the premises and on the houses to be erected thereon. To induce the plaintiff to accept this security as payment, the obligors represented and warranted that each of these fifty-two lots would be improved with a building and other improvements in accordance with the plans and specifications. The condition of the bond was that if within ten months from its date, October 13, 1927, each of the fifty-two lots should be fully improved and completed with a building together with other improvements in accordance with the plans and specifications, then the bond should be void, otherwise it should remain in full force and effect in law.

The case was tried before Judge William H. Kirkpatrick without a jury. In addition to the facts recited, Judge Kirkpatrick found them to be in brief as follows: Copley Homes Inc. immediately began building fifty-two houses on the lots. On August 13, 1928, the date for completion fixed by the bond, twenty-four houses had been fully completed. The remaining twenty-eight houses had not been completed either fully or substantially. The operation was, however, ultimately completed by the holder of

the first mortgages on December 27, 1929, as a result of a settlement with the defendant. Immediately thereafter the holder of the first mortgage foreclosed, buying in all the properties for the sum of $50.00 and thus wiping out the equity of The Trainor Company in the second mortgage. The plaintiff has received in all $13,026.02 from Copley Homes Inc. on account of its obligation to pay $28,000 with interest.

The Court further found that on August 13, 1928, the date fixed for completion by the defendant's bond, the value of the twenty-eight uncompleted houses was $6700 each. This amount was, very slightly, in excess of the amount of the plaintiff's mortgage on each house and all prior liens. On that date the completed houses were worth $7950 each. Subsequent to August 13, 1928, the total sum of $26,071 was spent in completing the operation. During 1928, 1929 and 1930 the value of real estate generally and in the locality in which this operation was, declined steadily. It is not disputed that at the time of the breach of the bond The Trainor Company could not under the terms of the mortgage protect itself by foreclosure.

On the basis of those facts the learned Trial Judge reached the following conclusions of law relevant to the issues:

He held that the bond was a bond of guaranty and not of indemnity and that there having been a breach, the plaintiff was entitled to judgment. He further held, however, that there is no substantial difference in the measure of damages upon the breach of a bond of guaranty and the breach of a bond of indemnity and that on a guaranty bond the plaintiff must show loss or else be limited to nominal damages, and that, since the value of the property in the condition in which it was left was equal to the sum of the

plaintiff's mortgage debt as well as prior liens, the plaintiff's mortgage was protected and it was entitled to nominal damages only.

In reaching these conclusions, as will be apparent by perusal of the opinion of the learned Trial Judge (49 F. (2d) 769), the learned Trial Judge believed that he was following the law as laid down by the Supreme Court of Pennsylvania and did not attempt or purport to lay down a different rule for the Federal Courts opposed to the State law.

An appeal was taken by the plaintiff to the Circuit Court of Appeals for the Third Circuit. After the appeal was taken but before it was argued, two cases were decided by the Supreme Court of Pennsylvania squarely covering the question of the measure of damages on the breach of a bond given to a mortgagee-obligee guaranteeing the completion of a building. In both opinions the Supreme Court squarely held that the conclusion reached by the learned Trial Judge in the instant case as to the measure of damages was not the law of Pennsylvania.

In MECHANICS TRUST CO. v. FIDELITY AND CASUALTY Co., 304 Pa. 526, 535, Mr. Chief Justice Frazer held "The measure of damages on a bond given to a mortgagee-obligee guaranteeing completion, is the cost of completion . . . *and is not limited to the difference between the value of the property in the condition in which it was left and the amount of principal and interest due on the mortgage.*"

In PURDY v. MASSEY, 306 Pa. 288, a case which presented strong equities on behalf of the defendant, both the lower court and the Supreme Court had the opinion of the learned Trial Judge in the instant case strongly urged

upon them and specifically refused to follow it, declaring the proper measure of damages to be that laid down by Mr. Chief Justice Frazer in Mechanics Trust Co. v. Fidelity and Casualty Co., *supra*.

Both of these cases, as well as cases to the same effect from other jurisdictions, were urged by the Appellant upon the Circuit Court of Appeals. The Circuit Court of Appeals, however, in its opinion affirmed, in effect, upon the opinion of the court below. In its opinion the Court did not refer to the opinion of Mr. Chief Justice Frazer in Mechanics Trust Co. v. Fidelity and Casualty Co., *supra*, but concluded

> "We do not regard the decision in Purdy v. Massey as creating a new local law of Pennsylvania but that, at most, it declared the common law of that state (as those terms are used in the two decisions last cited) with respect not to property but to the subject of suretyship, which from its very nature is general law running, like commercial law, broadly through all the states. In such case 'where the common law of the state is derived from the principles of general jurisprudence common to all the states' a federal court may (as we have done) exercise an independent judgment as to what is the law without respect to the decision of the state court as binding authority.
>
> "We are of opinion the Court below committed no error in holding that when on August 13, 1928, Trainor's mortgage was protected and, therefore, it committed no error in restricting the judgment to nominal damages."

THE QUESTIONS INVOLVED.

1. Was the court below correct in holding that there is no substantial difference in the measure of damages for the breach of a bond giving an absolute guaranty of completion and an indemnity bond?

2. Was the lower court correct in holding that the measure of damages on a bond given to a mortgagee-obligee guaranteeing completion is the difference between the value of the property in the condition in which it was left and the amount of principal and interest due on the mortgage and prior liens?

3. Was the lower court correct in holding that the issue presented by the instant case is one of suretyship rather than a question of the measure of damages?

4. Was the lower court correct in holding that the question here involved is a matter of general law concerning which a Federal Court may exercise an independent judgment as to what is the law without respect to the decision of the State court as binding authority?

5. Where there is a definite clearly enunciated principle of commercial law laid down by the court of last resort of a state, should the Federal Courts adopt a diametrically opposite view unless compelled thereto by potent reasons of policy or legal soundness?

6. Was the Circuit Court of Appeals correct in holding that on the facts as found by the learned Trial Judge The Trainor Company's mortgage was protected and it, therefore, was entitled to nominal damages only?

REASONS FOR GRANTING THE WRIT.

1. Because the judgment of the Circuit Court of Appeals in affirming the ruling of the lower court that there is no substantial difference between the measure of damages for the breach of a bond giving an absolute guaranty of completion and an indemnity bond establishes a rule on a question of fundamental legal importance that is not only directly in conflict with the established law of Pennsylvania, but also directly contrary to the law on that point as stated by your Honorable Court. This rule is also irreconcilable with earlier decisions by the same court and with the rule as laid down by the texts. No authority is cited by either the District Court or the Circuit Court of Appeals to support this ruling nor has counsel been able to find any such authority.

2. Because the measure of damages applied by the Circuit Court of Appeals in affirming the District Court has been explicitly disavowed by the Supreme Court of Pennsylvania and is in direct conflict with the rule applied by the Court of Appeals of New York State and the question is one of fundamental importance in the construction of all bonds.

3. Because in holding that the question of law presented by the instant case is a matter of general law concerning which a Federal Court may exercise an independent judgment without respect to the decision of the State courts, the Circuit Court of Appeals is directly in conflict with the decisions of the Circuit Court of Appeals of the 2nd, 4th and 9th Districts.

4. Because the Circuit Court of Appeals in affirming the decision of the District Court has decided important

questions of general law in a manner that is untenable and is in conflict with a great weight of authority.

5. Because in holding that The Trainor Company's mortgage was protected in the instant case and that the plaintiff suffered nominal damages only, the Circuit Court of Appeals reached a conclusion in direct conflict with the decision to the Supreme Court of Pennsylvania and the Court of Appeals of New York State in closely analogous cases and one not tenable in view of the facts found by the learned Trial Judge.

WHEREFORE, your petitioner respectfully prays that a writ of certiorari be issued out of and under the seal of this Honorable Court, directed to the United States Circuit Court of Appeals for the Third Circuit, commanding that Court to certify and to send to this Court a full and complete transcript of the record and all proceedings of the said Circuit Court of Appeals in the said cause, to the end that the same may be reviewed and determined by this Court as provided by law, and that the said decree of the Circuit Court of Appeals may be reversed by this Honorable Court, and that your petitioner may have such other and further relief in the premises as to this Honorable Court may seem just and appropriate; and your petitioner will ever pray.

THE TRAINOR COMPANY,

By EDWARD E. DICKER,
Secretary.

DAVID L. ULLMAN,
JOSEPH J. BROWN,
Counsel for Petitioner.

STATE OF PENNSYLVANIA,
COUNTY OF PHILADELPHIA, } *ss.:*

EDWARD E. DICKER, being duly sworn according to law, deposes and says that he is secretary of The Trainor Company, petitioner herein, duly authorized to make this affidavit on behalf; that he has read and knows the contents of the foregoing petition, and that the same is true to his own knowledge, except as to the matters therein stated to be alleged on information and belief, and that as to those matters he believes it to be true.

EDWARD E. DICKER.

Sworn to and subscribed before me this seventeenth day of March, A. D. 1932.

CLARENCE A. GOSLIN,
(Seal) *Notary Public.*
Commission expires February 21, 1935.

CERTIFICATE OF COUNSEL.

We hereby certify that we have examined the foregoing petition. In our opinion the petition is well founded and the case is one in which the prayer of the petitioner should be granted by this Honorable Court. It is presented in good faith and not for delay.

JOSEPH J. BROWN,
DAVID L. ULLMAN,
Counsel for Petitioner.

IN THE

Supreme Court of the United States.

No. . October Term, 1932.

THE TRAINOR COMPANY,
Petitioner,

v.

THE AETNA CASUALTY AND SURETY CO.,
Respondent.

BRIEF IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI.

OPINIONS BELOW.

The opinion of the United States District Court for the Eastern District of Pennsylvania (Kirkpatrick, *D. J.*), rendered on February 13, 1931, appears at R. 31 and is reported in 49 F. (2d) 769. The opinion of the Circuit Court of Appeals, rendered on December 21, 1932, appears at R. 63 and is not yet officially reported.

JURISDICTION.

The judgment (order for mandate) of the Circuit Court of Appeals was entered January 25, 1933 (R. 69). The jurisdiction of this court is invoked under Section 240 (a) of the Judicial Code as amended by the Act of February 13, 1925 (43 Stat. 936, c. 229) and under Rule 38 of this court.

STATEMENT.

A statement of the facts and proceedings will be found in the petition.

SPECIFICATION OF ERRORS.

The Circuit Court of Appeals erred in the following respects:

1. In failing to reverse the ruling of the District Court that there is no substantial difference between the measure of damages for the breach of a bond giving an absolute guaranty of completion and for the breach of a bond indemnifying against loss for failure to complete.

2. In holding that "since the value of the property as of August 13, 1928 (the date of the breach) was more than the sum of the plaintiff's mortgage and prior leins, the plaintiff is not entitled to any substantial damages."

3. In failing to hold that the measure of damages due a mortgagee-obligee for the breach of a bond guaranteeing completion of an operation by a certain date is the difference between the value of the completed buildings which the obligee was guaranteed and the value of the buildings in the condition in which they were left, or so much thereof as is necessary to pay the plaintiff's mortgage in full; and is not limited to the difference between the value of the property in the condition in which it was left and the amount of principal and interest due on the mortgage and all prior liens.

4. In holding that the instant case presents a question of suretyship and not a question as to the proper measure

of damages for the breach of a bond guaranteeing the completion of a building operation.

5. In holding that the question presented in the instant case is one of general law in which a Federal Court may exercise an independent judgment without respect to the decisions of the State Court.

6. In failing to hold that the law of the instant case is governed by the decisions of the Pennsylvania Supreme Court in Mechanics Trust Co. v. Fidelity and Casualty Co., 304 Pa. 526, and in Purdy v. Massey, 306 Pa. 288.

7. In holding that the plaintiff's mortgage was protected on August 13, 1928 (the date when the bond guaranteed completion) and that, therefore, the plaintiff was entitled to nominal damages only.

ARGUMENT.

POINT 1.

There has long been a well-established and clear-cut distinction between an affirmative covenant for a specific thing and one of indemnity against damage by reason of the non-performance of the thing specified: PURDY v. MASSEY, 306 Pa. 288; WEIGHTMAN v. UNION TRUST Co., 208 Pa. 449. It is in ignoring this distinction that the District Court and the Circuit Court of Appeals fell into error in the instant case.

The rule is stated in 3 Sutherland "Damages" (4th Ed.), Section 765, "Where the contract is more than for an indemnity against damages, as where a party stipulates . . . for performance of any kind, the damages are not the gist of the action and the value of performance will measure the amount recoverable for the breach. The measure of damages . . . is the amount which would have been received if there had been a faithful performance."

In PURDY v. MASSEY in the opinion of the lower court, reported 15 D. & C. 485, the Court had before it the opinion of the District Court in the instant case and held

> "We are well satisfied, as we were before, that the bond of the Indemnity Insurance Company of North America given to the plaintiff, Elizabeth Purdy, in this case is a bond of guaranty and not a mere bond of indemnity against loss. The bond is an affirmative covenant for the doing of a specific thing, that is, the erection of the garage in question in accordance with the plans and specifications, and not a bond of indemnity merely against loss or damage by reason of the non-performance of that undertaking.

> "There is some confusion in the cases of other jurisdictions about the measure of damages to which obligees in both classes of these bonds are entitled, and in a very late case, on which counsel for the defendants places great reliance, TRAINOR CO. v. AETNA CASUALTY AND SURETY CO., 49 F. (2d) 769, the court expressed the opinion that there is no substantial difference in the measure of damages in these classes of bonds, holding that on a guaranty bond the obligee must show loss or else be limited to nominal damages, while on an indemnity bond, if he fails to show loss, he is out of court altogether. We do not understand that to be the law in Pennsylvania, so far as a guaranty bond is concerned. It has been stated quite to the contrary."

This opinion was affirmed by the Supreme Court in 306 Pa. 288. The Supreme Court had before it precisely the same arguments that were presented to the Circuit Court of Appeals in the instant case. An examination of the briefs filed on behalf of the Aetna Casualty and Surety Company in the present case and on the Indemnity Insurance Company of North America, Appellee, in PURDY v. MASSEY, will show that the two briefs are practically verbatim the same from cover to cover. The Supreme Court of Pennsylvania having that argument before it in an opinion by Mr. Justice Drew held

> "*The basic question in this case is whether or not the bond in suit is one of guaranty or indemnity.* The action is assumpsit on a completion bond; the lower court held it to be a guaranty, and the measure of damage thereon to be the cost of completion. . . . In the instant case the bond guaranteed the completion of the building; if there had not been a breach of the obligation of the bond, the building would have been erected. Since this was not done, the plaintiff can only be put in as good a position as if the contract had been carried

> out by giving her the cost of construction, not exceeding, of course, the amount of the bond. The measure of damage on a bond guaranteeing completion is the cost of completion: EQUITABLE TRUST CO. v. NATIONAL SURETY CO., 214 Pa. 159; MECHANICS TRUST CO. v. FIDELITY & CASUALTY CO., 304 Pa. 526; BOARD OF EDUCATION v. MARYLAND CASUALTY CO., 27 Fed. (2d) 20."

To the same effect are WHEELER v. EQUITABLE TRUST CO., 206 Pa. 428; EQUITABLE TRUST CO. v. NATIONAL SURETY CO., 214 Pa. 159; WEIGHTMAN v. UNION TRUST CO., 208 Pa. 449; UNION TRUST CO. v. CITIZENS TRUST CO., 185 Pa. 217.

The District Court and the Circuit Court of Appeals seem to distinguish these cases on the ground that the obligee in the instant case is a mortgagee and not an owner, but in every one of the cases cited above the obligee was the mortgagee, and it is, therefore, submitted that it is the nature of the bond and not the status of the obligee which determines the liability.

The distinction between an obligation to do a specific thing and an obligation to indemnify against loss for failure to perform has long been recognized in the Federal Courts: WICKER v. HOPPOCK, 73 U. S. 94. There the distinction between the two bonds is carefully considered and the measure of damages for the breach of a contract to pay or perform as distinguished from a contract to indemnify is stated to be the amount which would have been received if the contract had been kept and not broken. To the same effect is CUDABACK v. HAY, 134 Fed. 120, in an opinion by the U. S. District Court for the Eastern District of Pennsylvania which was affirmed by the Circuit Court of Appeals for the Third Circuit in 139 Fed. 369.

The same rule is laid down by the New York Court of Appeals in BELLONI v. FREEBORN, 63 N. Y. 383, and KIDD v.

McCormick; 83 N. Y. 391; and in United Real Estate Co. v. McDonald, 140 Mo. 605; 41 S. W. 913. The textbook writers unanimously support the same rule.

31 Corpus Juris, page 420, Section 7;

14 R. C. L. 57;

16 Am. & Eng. Cyc. Law (2d Ed.) 179.

The only case cited by either the District Court or the Circuit Court of Appeals to support the rather revolutionary view set forth by the District Court is Swartz v. Ainwell Co., 227 N. Y. 184. In regard to this case, it is to be observed that in the first place this was a four to three decision with Justices Cardozo and Pound among the dissenting Judges. In the second place Swartz v. Ainwell is not authority for the rule which it is cited as supporting. A careful reading of the case and a perusal of the synopsis of counsel's briefs preceding the opinion in the report, will make it clear that what was there decided was not the proper measure of damages on a guaranty bond, but whether the bond there under consideration was in fact a guaranty or an indemnity bond. The majority of the Court decided that the purpose of this bond was to indemnify and that therefore, actual loss must be shown. It is respectfully submitted that the proper measure of damages for the breach of a bond guaranteeing performance is the amount which would have been received if there had been a faithful performance and that the Circuit Court of Appeals erred in refusing to so hold.

Point 2.

The law governing the proper measure of damages for the breach of a bond given to a mortgagee-obligee guaranteeing completion is so fully covered by the recent Pennsyl-

vania opinions in MECHANICS TRUST CO. v. FIDELITY & CASUALTY Co., 304 Pa. 526, and in PURDY v. MASSEY, 15 D. & C. 485 and 306 Pa. 288, and the facts in those cases are so closely analogous to the facts in the present case that to refer to them adequately would require quotation practically in full.

The contention of the defendants in each of these cases was precisely the same as the contention of the defendant in the instant case and it is worthy of note that in MECHANICS TRUST Co., *supra*, Mr. Chief Justice Frazer postulated a conclusion of nominal damages under the facts in the instant case as being a reductio ad absurdum conclusively establishing the fallacy of the measure of damages contended for by the defendants in all three cases and adopted by the Circuit Court of Appeals in the instant case.

In PURDY v. MASSEY, in both the lower court and the Supreme Court, the Court had before it the opinion of the learned District Judge in the instant case and specifically refused to follow it. The lower court after considering the opinion stated, "We do not understand that to be the law in Pennsylvania, so far as a guaranty bond is concerned. It has been stated quite to the contrary," and the Supreme Court in its opinion by Mr. Justice Drew cited the instant case as an example of a plain and unambiguous covenant to do a specific thing where there could be no doubt that the bond was one of guaranty.

POINT 3.

The basic rule establishing the measure of damages for a breach of a covenant to do a specific thing is that laid down by your Honorable Court in WICKER v. HOPPOCK, 73 U. S. 94, where it was held "that on the breach of a contract to

pay or perform as distinguished from a contract to indemnify, that which would have been received if the contract had been kept is the measure of damages if the contract is broken." Applied to the facts in the instant case, the Pennsylvania Supreme Court has declared the measure of damages to be the cost of completion. As is pointed out in a very able opinion by the Court of Appeals of New York in KIDD v. MCCORMICK, 83 N. Y. 391. "Stated in its broadest form, the plaintiff is to have that compensation which will leave him as well off as he would have been if the contract had been fully performed. With more particularity he has a right to a house as good as that which the defendants agreed to furnish; and his damage is the difference between the value of the house furnished and the house as it ought to have been furnished." As the New York Court of Appeals points out, that difference in value may be measured by the cost of completion. In none of the cases heretofore referred to has the cost of completion—or the difference in value between the completed and the incompleted houses—been greater than the amount of the mortgage and that situation has, therefore, not been discussed. In the instant case, both the cost of completion and the difference in value are substantially greater than the unpaid balance of the plaintiff's mortgage. The plaintiff, applying to the facts of the instant case the fundamental rule that they are entitled to receive only that which they would have obtained if the contract had been kept and not broken, claim only so much of the cost of completion—or difference in value—as would suffice to pay their mortgage in full. This is not, as the District Judge seemed to think, a departure from the measure of damages contended for by the plaintiff and laid down in the cases cited but merely an application of that principle to the facts of the instant case.

POINT 4.

The Circuit Court of Appeals held in its opinion (R. 63) that the opinions of the Supreme Court of Pennsylvania declared the common law of Pennsylvania with respect not to property but with the subject of suretyship, which from its very nature is a general law, running like commercial law broadly through all the states.

It is respectfully submitted that the question here at issue is not a question of suretyship but one of the measure of damages for the breach of a bond. The bond (R. 9) is a joint and several bond of the builder and the defendant. The plaintiff has elected to sue the defendant. No question peculiar to the law of suretyship is presented. It happens that the defendant was a surety on the bond but that is purely accidental and incidental. Precisely the same issues would be presented if the suit were against the principal and the issue presented is to determine the proper measure of damages for the breach of a bond guaranteeing the completion of a building.

POINTS 5 AND 6.

It is respectfully submitted that whether the instant case is regarded as presenting a question of suretyship or of the measure of damages that the decisions of the State Court of last resort should be followed by the Federal Courts. It should be noted that the instant case deals with a bond executed in Pennsylvania and to be carried out in that State; that the giving of the bond was a condition precedent to the conveyance by the plaintiff of real estate owned by it here and was aimed to protect a mortgage on that real estate; that suit was originally instituted in the courts of Pennsylvania and that the present issue finds

itself in the Federal Courts only because of the somewhat synthetic citizenship of the defendant corporation. No federal question is involved. The law invoked is of local character. The distinction between a bond guaranteeing the performance of an act and an indemnity bond has long been well established in Pennsylvania and that distinction has previously been recognized and followed by the District Court of this district and the Circuit Court of Appeals for the Third Circuit: CUDABACK v. HAY, 134 Fed. 120, affirmed 139 Fed. 369. All these facts may be presumed to have been in the minds of the parties when the bond was executed, for, as is pointed out in MECHANICS TRUST CO. v. FIDELITY & CASUALTY CO., 34 Dauphin Co. Rep. (Pa.) 47, the premium paid to the surety company for a bond of guaranty is substantially greater than that paid for a bond of indemnity and it may, therefore, be assumed that both parties believed that the plaintiff was getting greater protection under the form of bond executed in the instant case.

In other circuits it is well determined that in the construction of surety bonds and in determining the measure of damages, the Federal Courts will follow the rule laid down by the State Courts. In COMMUNITY BUILDING v. MARYLAND CASUALTY CO., 8 Fed. (2d) 678, the Circuit Court of Appeals of the Ninth Circuit had before it a bond given by a surety company guaranteeing the completion of a dormitory by a certain date. The contractor abandoned work and the plaintiff completed the job and brought suit for the cost of completion. The District Court there held that while under the State law the plaintiff was entitled to recover, under the Federal rule it had forfeited that right by failure to promptly notify the surety company of the contractor's breach. After a very careful consideration of the authorities, the Court held

> "From the foregoing consideration we reach the conclusion that in determining the rights of litigants arising out of a contract of suretyship such as this one, made and to be performed in the State of Washington, the Federal Court should follow the rule established by the highest court of that state."

It, therefore, reversed the judgment and remanded the case to the court below with instructions to enter judgment in favor of the plaintiff in the amount to which it was entitled.

In STURTEVANT COMPANY v. FIDELITY AND DEPOSIT COMPANY, 285 Fed. 367, the Circuit Court of Appeals of the Second District held that in construing a bond given by a school contractor it should follow the State rule.

In MULLINS LUMBER CO. v. WILLIAMSON & BROWN LAND & TIMBER CO., 255 Fed. 645, the Circuit Court of Appeals for the Fourth Circuit held that the measure of damages for the taking of timber was determined by the State law, and in HUGHES FEDERAL PRACTICE, JURISDICTION AND PROCEDURE (1931), Volume 6, Section 3735, Page 375, the rule is laid down "The Federal Courts follow the law of the State in which they are sitting, as declared by the State Courts, in respect to damages in actions at law." In note 41, a number of cases are cited supporting this statement. Among them is a decision of the District Court for the Eastern District of Pennsylvania in AMERICAN ICE COMPANY v. POCONO SPRINGS ICE COMPANY, 179 Fed. 869, affirmed by the Circuit Court of Appeals for the Third Circuit in 183 Fed. 193.

The general principles upon which the plaintiff's position rests could not be better stated than has been done by

the learned Judges of the Circuit Court of Appeals for the Third Circuit in McLain v. Provident Saving Life Assurance Society of New York, 110 Fed. 80, 91.

> "In extending the judicial power of the United States to controversies between citizens of different states the only purpose indicated by the constitution was to provide another forum than that of the state, not another law than that of the state. In this case the court below was exercising its jurisdiction concurrent with that of the court of the state of Pennsylvania. It was administering the laws of that state and was as much bound by its statutes and common law and its declared public policy as would the state courts in a like case."

As is further pointed out by Judge Dickinson in Warren County v. Southern Surety Co., 34 Fed. (2d) 168, 170 (Eastern District of Pennsylvania)

> "One practical obstacle to the following of different rulings in the State and United States Courts, and diversity of citizenship cases, is that the law varies with accident of residence and the sum in controversy. This should not be. The law should be uniform in its operation irrespective of the parties or financial interest at stake."

The present case is not a case where the Federal Courts have before them a series of decisions laying down a Federal rule as opposed to a State rule in the premises and feel bound by the principle of stare decisis. The only analagous case in this jurisdiction is Board of Education v. Maryland Casualty Co., 27 F. (2d) 20 (C. C. A. 3d), where the Court held that the measure of damages for the breach of a bond guaranteeing completion was the cost of construction.

This opinion was cited by Mr. Chief Justice Frazer in MECHANICS TRUST CO. v. FIDELITY & CASUALTY CO., *supra,* as supporting the Pennsylvania rule. In the argument of PURDY v. MASSEY, *supra,* it was urged upon the Pennsylvania Supreme Court in precisely the same language employed by the defendant in this case that this opinion should be distinguished because there the obligee was an owner and not the mortgagee and yet Mr. Justice Drew in PURDY v. MASSEY again cited BOARD OF EDUCATION v. MARYLAND CASUALTY CO. as being in accord with the Pennsylvania rule. It should be further noted that in his opinion in the BOARD OF EDUCATION case, Judge Woolley makes no distinction between a mortgagee-obligee and an owner-obligee but on the contrary, cites and relies upon UNITED REAL ESTATE CO. v. MCDONALD, 140 Mo. 605, which is a mortgagee-obligee case on all fours with the facts in the instant case.

It is, therefore, respectfully submitted that in holding that the Federal Courts were under no obligation to follow the State Courts on the facts presented by the instant case, that the Circuit Court of Appeals for the Third Circuit fell into error and that this error should be corrected before it becomes imbedded in the law. The practical result of having conflicting rules in the State and Federal Courts governing bonds guaranteeing the completion of building operations cannot but be detrimental to the entire building industry and confusing to a degree. The revival of building operations is essential to the country's prosperity. A safe and secure method of financing such operations is in turn essential to the revival of building activities. It is an anomaly to have a bond couched in the same language construed in one way in the State Courts and in a diametrically

opposite way in the Federal Courts. Whether a person can recover upon the breach of such a bond will then depend upon whether the defendant company happens to be a Pennsylvania corporation or a foreign corporation doing business in Pennsylvania, or upon whether the amount of damages incurred is more or less than $3000. Unless the owners of property feel that they are getting real protection and not merely nominal protection they will not be willing to subordinate purchase money mortgages to construction mortgages as was done in this case and as is a very common method of financing building operations in Pennsylvania. To make this procedure uncertain and fraught with danger for the owner of the real estate cannot but have unfortunate results.

POINT 7.

The Circuit Court of Appeals erred in holding that the plaintiff's mortgage was in fact protected on August 13, 1928, and that, therefore, the plaintiff was entitled to nominal damages only.

It is respectfully submitted that judicial decisions must correspond to the actual facts of business life and that in so far as they do not do so they stand self-indicted. To hold that the plaintiff, holding as it did a junior lien in a second mortgage secured upon a building operation more than half of which was incomplete was in fact protected, is to fly in the face of the conceded facts and in the face of the everyday experience of all men having knowledge of the matters. True, the learned Trial Judge found that the value of the incompleted buildings was equal to the sum of the plaintiff's mortgage and all prior liens; but how could the plaintiff avail itself of that fact? Its mortgage was not in default; it could not sell the properties and thus

realize on the value which the Trial Judge found they had. Even if the plaintiff found a purchaser and produced him to the owner, the owner was under no obligation to sell for a sum equal to the face of the mortgages only and renounce his investment in the buildings and all hope of profit, nor was there any way in which the plaintiff could compel the owner to sell. If the owner elected to sit by, as it did in this case, hoping to find funds to complete, hoping that the real estate market would rise, hoping somehow to make a profit, there was nothing that the plaintiff could do to protect itself. In the meantime, as found by the learned Trial Judge, real estate values were continually declining. Interest on prior liens was accumulating, taxes were piling up, insurance premiums had to be paid. The partially completed buildings were standing exposed to the action of the weather and to deterioration.

Incompleted houses cannot be rented, can produce no income with which to meet these carrying charges which are constantly accruing. It is a matter of which the Court should take judicial notice that it is difficult, if not impossible, to find a purchaser for a partially completed structure even though a completed house in the same location may be readily saleable. All these things the parties knew and it was to protect the plaintiff against precisely this situation that the bond in suit was entered into. To hold that a second mortgagee under these circumstances is adequately protected is to follow a theory and to ignore the actual situation and results in a conclusion which cannot possibly be justified by the admitted objective facts.

The plaintiff had contracted to get and the defendant had guaranteed to give it, not an incompleted house worth the sum of mortgages on the date of the breach but worth

less every day thereafter, but a completed structure capable of yielding a revenue which would meet the carrying charges and prevent a foreclosure because of a default in prior liens. The plaintiff had parted with its land upon the defendant's guarantee that it would be given as security for its mortgage completed buildings by a certain date. That was the security stipulated for. That was the contract made by the parties, and the Courts have no right to compel the plaintiff to accept in lieu of the security contracted for an entirely different and manifestly inferior protection. The actual inadequacy of the security of incompleted houses is well pointed out in the opinion of the New York Court of Appeals in KIDD v. MCCORMICK, 83 N. Y. 391, and is well illustrated by the actual course of events in the instant case.

If the contemplated houses had not been marketable the plaintiff's loss would have been incurred through its own bad business judgment and it could have no ground for complaint. But the completed houses were readily marketable for $7950, $1250 more than the sum of the mortgages and all liens. If the defendant's obligation had been kept and not broken, the plaintiff would have been paid in full. But the defendant's obligation was not kept. Instead of completed houses worth $7950, it was given as security incompleted houses worth $6700 and which could produce no revenue to meet the constantly accruing charges. The plaintiff was forced to sit by helpless while mortgage interest, unpaid taxes and insurance premiums accumulated, while the real estate market steadily dropped, until finally the operation was foreclosed upon by the holder of the first mortgage and the plaintiff's equity was entirely wiped out. How could it be said under these facts that the plaintiff has suffered nominal damages only?

The fallacy of the conclusion reached by the Circuit Court of Appeals is further pointed out in the opinion of Mr. Chief Justice Frazer in MECHANICS TRUST CO., *supra,*

> "Defendant company . . . argues that its liability should be measured by the difference between the value of the property in the condition in which it was left by Turby and the amount of principal and interest due on the mortgage. This theory proceeds upon the erroneous assumption that the bank loaned the $15,000 to Turby solely upon the bond and mortgage executed on February 7, 1928. At the time plaintiff loaned the money, it took an obligation on land upon which four completed houses *were to be built.* The mortgage was upon land and completed houses. The bank was not satisfied with the security of the bond and mortgage so long as the houses were not in existence and consequently required Turby to give it additional security of a bond guaranteeing that the houses would be built. Defendant company became surety on Turby's bond that completion of the building would take place. Plaintiff had a right to require the personal surety bond in addition to the other security, and defendant, being paid for the suretyship, was obliged to know the legal effect of its obligation at the time it became surety. Plaintiff, by this bond, protected itself against the possibility of breach by Turby; i. e., the possibility of his not enhancing the value of the premises as he had promised to do. Plaintiff was entitled to have the buildings completed, and the damage to it occasioned by the breach, in so far as concerns the surety on its bond, was the reasonable value of completion."

CONCLUSION.

It is respectfully submitted that in holding that there is no substantial difference as to the measure of damages between a bond guaranteeing the performance of an act and a bond indemnifying for non-performance that the Circuit Court of Appeals has taken a position opposed to the almost unanimous weight of authority.

The direct conflict between the rule adopted in the instant case and the rule applied by the Supreme Court of Pennsylvania cannot but result in uncertainty and confusion and be detrimental to the public interest which is directly concerned in making possible the revival of the building industry.

The conclusion of the Circuit Court of Appeals that in questions of suretyship, or more properly speaking, measure of damages in actions of law, the Federal Courts may exercise their independent judgment without respect to the decisions of the State Courts, is directly contrary to the conclusions reached by the Circuit Courts of Appeals in the Second, Fourth and Ninth Circuits and this conflict of opinion should be resolved by your Honorable Court.

The conclusion of the Circuit Court of Appeals that the plaintiff was protected because the incompleted buildings were worth the sum of the mortgages as of the date of the breach is directly contrary to the conclusion reached by the New York Court of Appeals in KIDD v. MCCORMICK, *supra*, and by the Pennsylvania Supreme Court in MECHANICS TRUST CO. v. FIDELITY & CASUALTY CO. and PURDY v. MASSEY, and furthermore cannot be sustained in view of the admitted facts.

The petition for writ of certiorari should be granted.

Respectfully submitted,

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